

## **Legislative Framework for a Washington Cap and Trade Bill**

### **Sections**

#### **1) Legislative Intent and findings**

- a. Overall description of climate change concerns voiced by the legislature
- b. Intent to create a market-based program to achieve the statewide emissions goals as defined in RCW 70.235.020
- c. Intent to use the most cost-effective market-based program to reduce greenhouse gas emissions measured by \$ per unit of GHG reduction
- d. Intent to minimize impacts on Washington households, consumers and businesses

#### **2) Definitions**

- a. "Allowance" means a tradable authorization to emit up to one metric ton of carbon dioxide equivalent.
- b. "Allowance price containment reserve" means an account maintained by the department with allowances available for sale through separate reserve auctions at predefined prices to assist in containing compliance costs for covered and opt-in entities in the event of unanticipated high costs for compliance instruments.
- c. "Annual allowance budget" means the total number of greenhouse gas allowances allocated for auction or distribution for one calendar year by the department.
- d. "Auction" means the process of selling greenhouse gas allowances, along with allowances from external greenhouse gas emissions trading programs with which Washington has linked its carbon pollution market program, by offering them up for bid, taking bids, and then distributing the allowances to winning bidders.
- e. "Auction ceiling price" means the maximum price for allowances that would be accepted for bids at auctions.
- f. "Auction floor price" means a price for allowances below which bids at auction would not be accepted.
- g. "Auction purchase limit" means the limit on the number of allowances one registered entity or a group of affiliated registered entities may purchase from the share of allowances sold at an auction.
- h. "Aviation fuel" has the same meaning as provided in RCW 34 82.42.010.
- i. "Biofuels" means a fuels derived from non-fossilized and biodegradable organic material originating from biogenic plants, and animals, or microorganisms, material, especially including: products, by-products, residues and waste from agricultural, or forestry, waste products, and related industries; the non-fossilized and biodegradable organic fractions of industrial and municipal wastes; and gases and liquids recovered from the decomposition of non-fossilized and biodegradable organic material.

- j. "Carbon dioxide equivalent" (CO<sub>2</sub>e) means a measure used to compare the emissions from various greenhouse gases based on their global warming potential.
- k. "Compliance instrument" means an allowance or offset credit, issued by the department or by an external greenhouse gas emissions trading program to which Washington has linked its carbon pollution market program. A covered or opt-in entity may use one compliance instrument to fulfill each compliance obligation equivalent to one metric ton of carbon dioxide equivalent.
- l. "Compliance obligation" means the requirement to turn in to the department the number of compliance instruments equal to a covered or opt-in entity's covered emissions during the compliance period.
- m. "Compliance period" means the three-year period for which the compliance obligation is calculated for covered entities except for the first compliance period. The first compliance period is from XXXX, through XXXXX
- n. "Covered entity" means a person with a compliance obligation, and who has emitted or is otherwise responsible, as specified in this chapter, for emissions that are more than the applicable emission threshold.
- o. "Department" means the department of ecology.
- p. "Emission threshold" means the greenhouse gas emission level at or above which a person has a compliance obligation.
- q. "Energy Intensive - Trade Exposed" or "EITE" means a manufacturing business that meets the numerical criteria established in section xx of this act, or has a proper primary North American industry classification system code as provided in section xx of this act
- r. "External greenhouse gas emission trading program" means a government program, other than Washington's carbon pollution market program created in this chapter, that controls greenhouse gas emissions from sources outside of Washington through an emissions trading program.
- s. "Facility," means any physical property, plant, building, structure, source, or stationary equipment located on one or more contiguous or adjacent properties in actual physical contact or separated solely by a public roadway or other public right-of-way and under common ownership or common control, that emits or may emit any greenhouse gas.
- t. "First jurisdictional deliverer" means the first person over which the state of Washington has jurisdiction that generates or procures electricity for use within the state and delivers that electricity to the first point of delivery.
- u. "General market participant" means a registered entity that is not identified as a covered entity or an opt-in entity who is registered in the program registry and intends to purchase, hold, sell, or voluntarily retire compliance instruments.

- v. "Greenhouse gas" means carbon dioxide (CO<sub>2</sub>), methane (CH<sub>4</sub>), nitrogen trifluoride (NF<sub>3</sub>), nitrous oxide (N<sub>2</sub>O), sulfur hexafluoride (SF<sub>6</sub>), hydrofluorocarbons (HFCs), perfluorocarbons (PFCs), and other fluorinated greenhouse gases.
- w. "Holding limit" means the maximum number of allowances that may be held for use or trade by a registered entity at any one time.
- x. "Imported electricity" means electricity generated outside the state of Washington and delivered for use within the state, but which did not originate from any jurisdiction with which Washington has a linkage agreement.
- y. "Limits" means the greenhouse gas emission reductions required for Washington state, as specified in RCW 70.235.020(1)
- z. "Linkage agreement" means a formal agreement that connects two or more carbon market programs to reciprocally recognize each jurisdiction's compliance instruments.
- aa. "Marine fuel" means a any fuel used to power an ocean-going vessel.
- bb. "Ocean-Going Vessel" means a commercial, government, or military vessel meeting any one of the following criteria:
  - i. A vessel greater than or equal to 400 feet in length overall (LOA) as defined in 50 Code of Federal Regulations (CFR) § 679.2, as adopted June 19, 1996;
  - ii. A vessel greater than or equal to 10,000 gross tons (GT ITC) pursuant to the convention measurement (international system) as defined in 46 CFR § 69.51-.61, as adopted September 12, 1989;
  - iii. A vessel propelled by a marine compression ignition engine with a per-cylinder displacement of greater than or equal to 30 liters.
- cc. "Offset credit" means a tradable compliance instrument that represents an emission reduction or emission removal of one metric ton of carbon dioxide equivalent.
- dd. "Offset project" means a project that reduces or removes greenhouse gases that derive from sources not covered by the program.
- ee. "Offset protocols" means a set of procedures and requirements to quantify greenhouse gas reductions or greenhouse gas removals achieved by an offset project.
- ff. "Opt-in entity" is a person responsible for the emission of greenhouse gases not covered by the program and that voluntarily chooses to participate in the program as if it were a covered entity.
- gg. "Person" means an individual, firm, partnership, franchise holder, association, organization, corporation, business trust, company, limited liability company, or government entity.
- hh. "Point of delivery" means a point on the electricity transmission or distribution system physically located in Washington where a power supplier delivers electricity for use in the state. This point can be an interconnection with another system or a substation where the transmission provider's transmission and distribution systems are connected to another system, or a distribution substation where

electricity is imported into the state over a multijurisdictional retail provider's distribution system.

- ii. "Program" means the carbon pollution market program implemented under this chapter.
- jj. "Program registry" means the data system in which covered entities, opt-in entities, and general market participants are registered and in which compliance instruments are recorded and tracked.
- kk. "Registered entity" means a covered entity, opt-in entity, or general market participant that has completed the process for registration in the program registry.
- ll. "Retire" means to permanently remove an allowance or offset credit such that the allowance or offset credit may never be sold traded, or otherwise used again.
- mm. "Surrender" means to transfer an allowance or offset credit to the department, either to meet a compliance obligation or on a voluntary basis.

### 3) Creation of Program

- a. To achieve the statewide emissions goals as defined in RCW 70.235.020, this law establishes a market program to create and distribute allowances that can be traded in state and in other national or international programs that are linked
- b. The program shall include:
  - i. Creation of allowances
  - ii. Setting of an annual allowance budget
  - iii. Distribution of allowances to covered parties
  - iv. Identification of Energy Intense Trade Exposed businesses
  - v. An allowance auction process
  - vi. Allowance proceeds distribution process
  - vii. Allowance price containment provisions
  - viii. Offset credit mechanism to meet compliance obligations
  - ix. Linkage agreements with other jurisdictions
  - x. Creation of a compliance instrument tracking system
  - xi. A compliance requirement process

### 4) Scope of Coverage

- a. Stated intent that the program should cover all quantifiable GHG emissions in all sectors of the economy on a CO<sub>2</sub> equivalent basis
- b. Coverage to include all facilities above 25,000 tons CO<sub>2</sub>e/yr
- c. Coverage to include all in-state generated and imported electricity
- d. Coverage to include transportation fuel emission
- e. Coverage to include natural gas emissions not covered by large stationary sources

### 5) Exemptions

- a. Fuel brought into the state in the tank of a vehicle, vessel, plane
- b. Aviation fuel
- c. Marine fuel
- d. Biofuels

- e. Exported fuels, electricity and natural gas that are exported or flow through the state
- f. Emission previously covered by an out-of-state carbon policy, charge, tax or regulation
- g. Fuels consumed by EITE designated facilities

6) Setting the Cap

- a. The department of revenue shall establish an annual cap
- b. The cap shall be set in a manner that will achieve the statewide emissions goals as defined in RCW 70.235.020
- c. The cap decline factor will be set at the start of the program and be calculated as a level amount for each year based on a calculation of the 2035 emissions goal defined in RCW 70.235.20 less the most recent level of recorded emissions in the state then divided by the number of years between the commencement of the program and December 31, 2035.

7) EITE discussion and protection

- a. A party shall be an EITE if it is
  - i. List of EITE's from Carbon Tax, or
  - ii. Is an EITE as calculated by the following formula

The department of commerce will apply objective numerical criteria for both energy intensity and trade exposure for the purpose of identifying energy-intensive trade-exposed manufacturing facilities. The criteria for energy-intensive trade-exposed status will be determined by applying the following methodology:

Induced Carbon Cost intensity = **(Direct Carbon Costs + Indirect Carbon Costs) / Gross Value Added**

Trade exposed = **(Import Value + Export Value) / (Import Value + Production Value)**

Where:

“Direct Carbon Costs” means the estimated maximum costs faced by a sector as a result of the implementation of the GHG Cap and Trade Program for the direct costs associated with direct emissions; i.e., stationary facility emissions not covered by offsets or rebates

“Indirect Carbon Costs” means the indirect costs faced by a sector associated with the cost of indirect emissions (emissions from electricity consumption) as the result of the potential increase in electricity prices as a result of the inclusion of electricity production in the scope of the GHG Cap and Trade Program.

“Gross Value Added (GVA)” means the aggregated value of goods and services produced in an industrial sector in Washington state as prescribed by the United Nations System of National Accounts (USNA); e.g., Gross Output - Intermediate Consumption

“Import Value” means the total gross value of imports within an industry sector due to production outside of Washington State

“Export Value” means the total gross value of exports within an industry sector sent to destinations outside of Washington State

“Production Value” means the total gross value within an industry sector from production within Washington State

“Export” means to transport a product from inside Washington State to persons or locations outside Washington State

“Import” means to bring into, introduce into, or land on any location subject to the jurisdiction of Washington State

A sector or subsector is deemed to be at a significant risk of carbon leakage and qualifies for EITE status if either:

- (i) the additional costs as a result of the implementation of the GHG Cap and Trade Program would lead to a cost increase exceeding 5% of its gross value added and
- (ii) trade intensity of the (sub-)sector concerned exceeds 10%, or
- (iii) if either of the two criteria in (i) and (ii) exceeds 30%.

A manufacturing business that can demonstrate to the department of commerce that its facility or facilities meet the criteria must be issued a certificate denoting energy-intensive trade-exposed status for the purpose of compensating appropriate on-site manufacturing processes through the issuance of free allowances.

(b)(i) Notwithstanding the criteria established in (a) of this subsection, the department of commerce must issue a certificate denoting energy-intensive trade-exposed status to:

(A) Any facility engaged in an activity described in RCW 18 82.04.260(12); or

(B) Any facility primarily engaged in an activity encompassed within any of the following North American industry classification system codes (2017):

112310: Chicken egg production;  
112320: Broilers and other meat type chicken production;  
112330: Turkey production;  
112340: Poultry hatcheries;  
112390: Other poultry production;  
212230: Copper, nickel, lead, and zinc mining;

311211: Flour milling;  
311221: Wet corn milling;  
311224: Soybean and other oilseed processing;  
311225: Fats and oils refining and blending;  
311230: Breakfast cereal manufacturing;  
311411: Frozen fruit, juice, and vegetable manufacturing;  
311412: Frozen specialty food manufacturing;  
311421: Fruit and vegetable canning;  
311422: Specialty canning;  
311423: Dried and dehydrated food manufacturing;  
311511: Fluid milk manufacturing;  
311512: Creamery butter manufacturing;  
311513: Cheese manufacturing;  
311514: Dry, condensed, and evaporated dairy product manufacturing;  
311520: Ice cream and frozen dessert manufacturing;  
311611: Animal (except poultry) processing;  
311612: Meat processed from carcasses;  
311613: Rendering and meat by-product processing;  
311615: Poultry processing;  
311710: Seafood product preparation and packaging;  
311812: Commercial bakeries;  
311821: Cookie and cracker manufacturing;  
311824: Flour mixes and dough manufacturing from purchased flour;  
311830: Tortilla manufacturing;  
311911: Roasted nuts and peanut butter manufacturing;  
311919: Other snack food manufacturing;  
311930: Flavoring syrup and concentrate manufacturing;  
311941: Mayonnaise, dressing, and other prepared sauce manufacturing;  
311942: Spice and extract manufacturing;  
311991: Perishable prepared food manufacturing;  
311999: All other miscellaneous food manufacturing;  
312112: Bottled water manufacturing;  
321212: Softwood veneer and plywood manufacturing;  
321213: Sawmills;  
322110: Pulp mills;  
322121: Paper (except newsprint) mills;  
322122: Newsprint mills;  
322130: Paperboard mills;  
324110: Petroleum refineries;  
324199: All other petroleum and coal manufacturing;  
325188: All other basic inorganic chemical manufacturing;  
325193: Biodiesel manufacturing;  
325199: All other basic organic chemical manufacturing;  
325311: Nitrogenous fertilizer manufacturing;  
327211: Flat glass manufacturing;  
327213: Glass container manufacturing;  
327310: Cement manufacturing;

327410: Lime manufacturing;  
327420: Gypsum product manufacturing;  
331110: Iron and steel mills;  
331312: Primary aluminum production;  
331313: Aluminum refining and primary aluminum production;  
331314: Secondary smelting and alloying of aluminum;  
331315: Aluminum sheet, plate, and foil manufacturing;  
331318: Other aluminum rolling, drawing, and extruding;  
334413: Semiconductor and related device manufacturing;  
336411: Aircraft manufacturing;  
336412: Aircraft engine and engine parts manufacturing;  
336413: Other aircraft parts and auxiliary equipment manufacturing;  
336414: Guided missile and space vehicle manufacturing;  
336415: Guided missile and space vehicle propulsion unit and propulsion unit parts manufacturing;  
336419: Other guided missile and space vehicle parts and auxiliary equipment manufacturing; and  
423930: Recyclable material merchant wholesalers.

(c) Facilities that have been designated as EITE will be protected from trade exposure by the issuance of allowances.

The allowances will be identified on a sector-by-sector basis and the sector as a whole shall receive free allowances at 90% of the liability imposed by the Cap and Trade Program. A declining cap adjustment factor shall be applied to this industry assistance

The Department of Commerce shall develop criteria that will ensure the distribution of the equivalent free allowances shall be based on a statewide benchmarking approach that does not disadvantage the most efficient operators by sector.

(d) Industry assistance to individual regulated entities shall be determined by a benchmarking approach that advantages the most efficient operators and that rewards early action. Under no circumstances shall a regulated entity receive less than XX% industry assistance.

(e) The industry assistance design shall remain constant for the duration of the program.

(f) A sector or subsector that has been designated as EITE shall be exempted from Cap and Trade program costs levied on fuels consumed by their facilities.

#### 8) Point of Regulation

- a. Compliance obligation should reside as close as possible to the point of emissions, providing transparency to emitters and helping them make economic choices to reduce emissions
- b. For transportation fuels, it should be applied at the rack

#### 9) Cost Containment



- a. Establish a price ceiling on the sale of allowances not-to-exceed \$80 in 2030 (in nominal dollars).
  - b. Establish two price containment points below the price ceiling, with the first point being set no lower than 1/3 of the value between the floor and ceiling price
  - c. Allow for the use of carbon offset credits, as defined in section 11, for up to 25% of a regulated entity's compliance obligation
- 10) Auction rules:
- a. Auctions should be held at a regular iteration throughout a calendar year according to a published schedule, with a minimum frequency of once per quarter,
  - b. The program administrator shall establish a process for the auctioning of current vintage allowances as well as future vintage allowances.
    - i. Current and future vintage allowances shall be auctioned separately.
    - ii. The auction of future vintage allowances shall not be subject to the holding limit
  - c. Each auction will be conducted with an auction reserve price and no allowances will be sold at bids lower than the auction reserve price
  - d. Holding limit shall be established for allowances with a vintage year corresponding to the current or previous calendar years
    - i. the holding limit will not include allowances contained in annual compliance accounts
  - e. Treatment of unsold allowances
  - f. Registration, disclosures
    - i. Ability to register as a consolidated corporate entity for direct corporate associations
- 11) Offsets
- a. Offset credits must result in reduction of GHG emissions that are real, permanent, verifiable, and additional
  - b. The program administrator shall prepare a list of approved offset protocols that are eligible to receive credit, but at a minimum, offset protocols approved by the state of California shall be eligible for crediting
  - c. The program administrator shall set crediting periods for the applicable offset protocols
  - d. Offsets generated in any US state, Canada or Mexico shall be eligible for crediting
  - e. The program administrator shall establish requirements for offset verification procedures and offset verification services
  - f. The program administrator must establish rules for determining offset credit invalidation
  - g. Allow for the banking of offsets

- 12) Compliance
  - a. Triennial Compliance Periods
  - b. Establishing of Accounts
  - c. Instruments eligible for compliance
    - i. Allowances of a vintage year equivalent to the compliance year or earlier
    - ii. Eligible offsets issued prior to the compliance deadline, up to 25% of the total compliance requirement
- 13) Preemption
  - a. No state agency, city, town, county, township, or any other subdivision or municipal corporation of the state may adopt or enforce a statewide or local program that sets a greenhouse gas emissions cap, limit, standard, regulation, reduction requirement, permit restriction (including carbon intensity)
  - b. The Clean Air Rule is repealed
- 14) Linkage
  - a. The department shall enter into linkage agreements with other jurisdictions with established market-based carbon emissions trading systems.
- 15) Legislative Oversight and Review
  - a. This act is repealed as of XXXXXX unless it is expressly reauthorized by the state legislature by that date. Legislative reauthorization may only take place after XXXXXX.